

**Senate Budget and Fiscal Review Subcommittee #4 on
Legislative, Executive, Judiciary, Transportation, and
General Government**

**Senator Joseph Dunn, Chair
Senator Dick Ackerman
Senator Denise Ducheny**

**Wednesday, April 30, 2003
2:30 p.m. or Upon Adjournment of
Banking, Commerce and International Trade Committee
Room 3191**

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Proposed Consent Calendar

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8620	Fair Political Practices Commission
8640	Political Reform Act of 1974
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Proposed Consent Calendar (Continued)

CONTROL SECTIONS

- 4.40 e-Business Center
- 4.80 State Public Works Board Interim Financing
- 6.00 Project Alterations Limits
- 9.20 Administrative Costs Associated with the Acquisition of Property
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- 12.30 Special Fund for Economic Uncertainties
- 24.30 Transfer School Building Rental Income to the General Fund
- 26.00 Intraschedule Transfers
- 27.00 Deficiency Reporting Requirements
- 28.00 Program Change Notification

Delete this Control Section per DOF request:

- 31.75 Augmentation pursuant to Control Section 31.70 Budget Act of 2002

0840 State Controller

The State Controller is responsible for (1) the receipt and disbursement of public funds; (2) reporting on the financial condition of the state and local governments; (3) administering certain tax laws and collecting amounts due the state; and (4) enforcing unclaimed property laws. The Controller is also a member of the Board of Equalization, the Franchise Tax Board, the Commission on State Mandates, the State Lands Commission, the Pooled Money Investment Board, and assorted bond finance committees.

The Governor's budget proposes expenditures of \$106 million (\$68 million GF) to support the activities of the State Controller's Office (SCO) in 2003-04. This is about one percent less than current-year expenditures. The budget proposes \$3.5 million from the General Fund and 32 new positions to implement Chapter 1128, Statutes of 2002 (AB 2834, Migden), to perform audits of local government mandate claims and other duties.

Issues

1. Unclaimed Property Program: Proposed Fees. Banks and other institutions are required to remit unclaimed property to the state. The most common types of unclaimed property are bank accounts, safe deposit box contents, stocks, and the proceeds of insurance policies. Property is deemed unclaimed when an account has remained dormant for three years and efforts by the institution holding the account to locate the owner have been unsuccessful. The unclaimed property is transmitted to the State Controller, who maintains records of all such property and attempts to identify the owners. Escheated property continues to belong to the owners of the unclaimed property, but the state is authorized to use the property while it is in the state's custody.

Interest is paid at the lower of 5 percent or the bond equivalent rate of the 13-week treasury bills on approved claims. The current interest rate is 1.69%.

The state currently holds \$3.2 billion in unclaimed property belonging to over five million individuals and organizations. The state receives about \$300 million annually in unclaimed property funds and returned \$190 million, including interest, to approximately 205,000 individuals and organizations in 2001-02.

The budget proposes expenditures of \$11.8 million (GF) and 140 positions to administer the unclaimed property program.

The budget proposes trailer bill language to deduct 3 percent of the unclaimed property value or \$10; whichever is greater, effective January 1, 2004. This charge is estimated to generate \$3 million in General Fund revenues in 2003-04 and \$6 million in 2004-05. This would cover about 55 percent of the costs of the program.

The trailer bill language also would extend the statutory deadline for the SCO to review unclaimed property claims from 90 days to 180 days. The language also eliminates a requirement that the Controller provide prior approval for payment through the national electronic payment system that transfers funds through federal reserve banks.

The LAO recommends amending trailer bill language to impose a fee on all approved claims at a level sufficient to cover administrative program costs. This would result in about \$5.4 million in revenues for 2003-04 and \$10.8 million in 2004-05—for General Fund savings of \$2.4 million in the budget year and \$4.8 million thereafter in comparison to the Governor's budget

The Controller has an alternative proposal to eliminate interest on the payment of claims instead of charging a fee. The estimated amount of interest to be paid in the budget year is \$12.0 million, or about the same as the administrative costs of the program. The Controller's proposal would take effect immediately upon enactment.

1730 Franchise Tax Board

The Franchise Tax Board (FTB) administers the Personal Income Tax and the Bank and Corporation Tax Laws, and the Senior Homeowners and Renters' Assistance program. In addition, FTB provides processing services through contracts with other governmental agencies and performs audits and field investigations of campaign statements and lobbyist reports authorized by the Political Reform Act. The board began collecting delinquent child support payments under a permanent program last year. FTB is funded at \$445.2 million, of which \$402.8 million is General Fund. This amount is \$16.5 million or 3.5 percent less than budgeted in the current year.

1. Integrated Non-Filer Compliance (INC). The INC program pursues taxpayers that do not file returns, but have tax liabilities over \$200. These individuals have income subject to taxes, but have not filed a tax return. A majority of the budget year reduction of \$16.5 million for FTB (\$11.8 million) is due to completion of the limited-term INC program.

The overall objective of FTB's non-filer compliance program is to ensure that businesses and individuals required to file tax returns in California carry out this obligation. The FTB's program uses a variety of automated and manual processes to achieve tax compliance from nonfilers. The INC program is part of this larger nonfiler compliance program operated by FTB. As part of this program, FTB receives federal tax returns from the Internal Revenue Service (IRS) for the last three years, wage information from the Employment Development Department, as well as various other data. By analyzing these data in an automated fashion, FTB can determine whether the records from these sources indicate that a federal return was filed or income was earned, and yet no state income tax return was filed.

The FTB has recently completed improvements to its nonfiler compliance program, resulting in cost savings and greater efficiencies. The new system will allow for the integration of more data into the system and lead to the identification of an additional 100,000 non-filers. The program is also expected to reduce unnecessary taxpayer intrusion by reducing the number of erroneous notices, assessments, and collection actions that have occurred in the past because of incomplete or inaccurate data.

The LAO recommends that the tax liability threshold be reduced from \$200 to \$100, which would result in FTB contacting an estimated 120,000 additional nonfilers. The FTB estimates that these additional contacts would generate an additional \$4.4 million in General Fund revenue in 2003-04. The overall cost of the expanded program would be \$800,000. This would have a benefit-cost ratio in excess of 5:1.

The 2002 May Revision proposed lowering the threshold to \$100, but the Legislature rejected this proposal.

2. E-File Tax Practitioner. The budget proposes trailer bill language to implement a program to require tax professionals who file 100 or more personal income tax returns to e-file or pay a fine of \$50 per return. This program would result in savings of \$1.4 million (GF) and 50.5 PYs. Tax practitioners filing returns for 100 or more taxpayers include about 10,000 of the 40,000 tax professionals who conduct business in California. These practitioners, however, prepare about 60 percent of the personal income tax returns filed.

The customer of a tax practitioner that prepares 100 or more tax returns would not have the choice of filing a hard copy of their return themselves. An identical proposal was rejected by the Legislature last year.

***The LAO recommends** amending the trailer language to require tax practitioners that file **50 or more** returns to e-file. Reducing the threshold to 50 or more returns would result in additional net annual savings of \$140,000 (5.5 PYs). There would be savings in administrative costs of \$400,000 offset by increased taxpayer assistance costs of \$260,000.*

Does the Subcommittee want to approve the trailer bill language?

3. Political Reform Audit Program. The budget proposes trailer bill language to change the funding for compliance audits from the General Fund to the Political Reform Audit Fund (newly created special fund). The trailer bill language would impose a fee on candidates filing for elected public offices, lobbyists, lobbying firms, lobbyist employers, and certain committees for deposit in the newly established fund.

It would not apply to committees that meet the following conditions:

- a) Make contributions totaling ten thousand dollars (\$10,000) or more in a calendar year to or at the behest of candidates or committees.
- b) Are controlled directly or indirectly by a candidate.

The trailer bill language does not specify the fee amount to be imposed. The fee would be imposed at the time of filing statements with the Secretary of State. The language requires the FTB to notify the Department of Finance biannually of the existing fee amount, the current fiscal year costs for the audit program, projected costs for the next two fiscal years, and the recommended fee amount for the next two years. The Director of Finance shall report on the amount of any fee increase no later than June 30, 2004 and biannually thereafter.

The new fee, although unspecified, is estimated to generate \$1.36 million to pay for the audit costs of the FTB. If this fee is not adopted, Item 8640 (Political Reform Act of 1974) must be augmented by \$1.36 million (GF).

Does the Subcommittee want to approve the trailer bill language?

4. Finance Letter: Penalty and Interest Waiver Program. The 2002-03 budget included an increase in collection staff of 34 one-year limited term positions at a cost of \$3.3 million to contact high-risk delinquent taxpayers with an offer to waive penalties and interest if back taxes are paid. This is not an amnesty program, but a settlement program to maximize revenue collection on a one-year basis. This was estimated to increase revenues by \$125 million in the budget year for a net gain of \$121.7 million (GF).

There is an April 1 Finance Letter requesting \$493,000 for continuation of the program for four additional months from September 1, 2003 through December 31, 2003. The additional four months are needed because the program started two months later than expected when the budget was approved. The current year allocation was reduced by \$308,000 in Chapter 3, Statutes of 2003-04 First Extraordinary Session (SB 19X).

If this appropriation is approved, how much revenue is expected to be collected?

Does the Subcommittee want to approve the Finance Letter?

4. Treasury Offset Program. Federal law provides for the collection of state tax obligations through a reduction of refunds payable to federal taxpayers. The federal government requires a reciprocal arrangement with states to offset certain federal obligations against state tax refunds. Currently, 25 states participate in the Treasury Offset Program (TOP).

The FTB performed a study in 1998 and determined that participation in TOP was not effective for the following reasons:

- The most appropriate application of TOP was to nonresidents, yet this was prohibited under the program.
- A significant portion of the balance due the taxpayer was already being offset by other obligations, such as child support, that are collected first.
- Procedural requirements, such as sending a certified letter of intent to all taxpayers potentially subject to the offset, were costly.

FTB concluded the program at that time was not cost-effective for California and that it was receiving better results from its existing collection activities than would be available through the TOP.

The LAO recommends that the FTB report regarding the feasibility and cost-effectiveness of participating in the existing Treasury Offset Program in order to reduce tax collection costs and increase revenues to the General Fund.

FTB should respond to the LAO recommendation.

5. Augmentation for Implementation of City Business Tax Disclosure. The budget requests increased reimbursement authority of \$355,000 and 4.4 PYs to implement Chapter 915, Statutes of 2001 (AB 63, Cedillo), which authorized FTB to disclose confidential tax information to city business tax officials. These costs will be fully reimbursed by the cities that use the information.

City tax officials use this information to identify individuals that report business income on state returns but do not have an active city business license within their city jurisdictional boundaries.

The Legislature denied a similar request for reimbursement authority for this chaptered legislation last year.

Does the Subcommittee want to approve the reimbursement expenditure authority?

1760 Department of General Services

The Department of General Services (DGS) provides management review and support services to state departments. The DGS is responsible for the planning, acquisition, design, construction, maintenance, and operation of the state's office space and properties. It is also responsible for the procurement of materials, data processing services, communication, transportation, printing, and security. The budget for DGS is proposed at \$837.1 million, of which \$3.0 million is General Fund. The total budget is about \$32 million or 3.7 percent less than in the current year. The General Fund support is reduced from \$110.2 million in 2001-02 and \$17.0 million in the current year to \$3.0 million in the budget year.

Issues

1. Rate Increase for the State Emergency Telephone Number Account (911 Account). Current law provides for a surcharge of up to 0.75 percent on intrastate calls. These funds can be used to pay refunds, administrative costs of the Board of Equalization and DGS for administering the surcharge, bills submitted to DGS by service suppliers or communications equipment companies for the installation and ongoing expenses for the 911 emergency phone number system, and claims of local agencies for approved incremental costs related to the 911 emergency phone number system.

Costs of DGS and local agencies that can be reimbursed are for the basic telephone system and approved incremental costs. Because the surcharge has a logical, direct relationship between the use or purposes and the persons from whom it was collected, the revenues collected are fees and not the proceeds of taxes.

The budget proposes trailer bill language to increase the surcharge on intrastate calls from 0.72 percent to one percent. This will increase revenues to this fund by \$46.6 million to a total of \$181.2 million. The use of the funds would be expanded to include the California Highway Patrol for providing 911 emergency assistance. The CHP is allocated \$41 million from this fund in the proposed budget. These revenues would replace existing funding sources.

This increase in the surcharge is considered a "tax" and not a "fee" because there is not a logical, direct relationship between the use or purposes and the persons from whom it was collected. This trailer bill language is considered a "change in state taxes for the purpose of increasing state revenues" and would require a two-thirds vote.

Should this trailer bill language be adopted?

2. Delegation of Authority. AB 3000 (a 2002 budget trailer bill) exempted DGS from various provisions in order to achieve improved levels of performance by focusing its efforts on enhancing the value of the services it delivers as a fee-for-service organization. These provisions are intended to assist DGS in providing services on a cost-competitive basis. This language sunsets at the end of the current year. Similar language has been included in budget trailer bills since 1995.

The budget proposes trailer bill language to make the following changes on a permanent basis:

- a) Delegate the authority to approve Architectural Revolving Fund transfers from DOF to DGS.
- b) Exempt DGS from filing an application of discharge with the SCO when it has been determined it is no longer cost effective to pursue collection efforts.
- c) Give DGS the option to procure goods usually purchased from the Prison Industry Authority from the private sector when it is cost beneficial to do so.
- d) Allow the Director of DGS, rather than the Director of DOF, to certify funds are available in the case of the department's liability for a legal settlement.
- e) Authorize the Director of DGS, rather than the Director of DOF to approve the deposit of checks into the Architectural Revolving Fund.
- f) Authorize the director of DGS, rather than the Director of DOF to certify funds for payment for all legal court settlements for projects funded from the Architectural Revolving Fund.

Should this language be made permanent?

3. State Printing Policy. In the 1995 budget act, the Office of State Printing (OSP) was authorized to offer printing services to state and other public agencies. In June 1996, the control that OSP has over print-procurement by state agencies was eliminated through a management memo from DGS. Printing jobs from the Governor's Office, the Legislature, and ballots were required to be performed by OSP. Thus, state agencies could obtain printing services through a bidding process.

In 1999, DGS mandated through a management memo that all state printing be done by a union shop. Later that year, DGS rescinded the written mandate. In October 2001, DGS reclassified agency print purchases as "personal service contracts". A state agency would be required to send all printing projects to OSP. OSP would have the choice of taking the job or contracting it out.

In 2002, AB 3000 provided that state printing procurement is not considered a personal service contract. The effect of this provision is that state departments are no longer required to submit all printing projects to OSP, but instead can obtain printing services through a bidding process that allows OSP also to bid on the project. This provision has no sunset.

AB 3000 also provided that that state departments would not be required to submit all printing projects to OSP, but instead could obtain printing services through a bidding process that would allow OSP to also bid on the project. This provision sunsets on the effective date of the 2003 Budget Act or June 30, 2003, whichever occurs later.

The budget proposes trailer bill language to extend this sunset to the effective date of the 2004 Budget Act or July 1, 2004, whichever is later. The statute is repealed as of January 1, 2005.

Should this language be adopted?

Should this language be made permanent?

4. Finance Letter: Procurement Training Program. This Finance Letter requests an on-going expenditure authority increase of \$1.5 million (Service Revolving Fund) for a new procurement training program for state employees. The training program is being developed by California State University (CSU) Northridge, and it consists of three component (1)\$480,000 to develop the training curriculum and courses, (2) \$840,000 for tuition and training sites costs, and (3) \$180,000 in CSU overhead costs. This would implement a recommendation of the Task Force on Contracting and Procurement Review. These activities would be funded by increasing the procurement service fees on departments by 5.6%.

The LAO recommends that the proposal be reduced by \$840,000 for tuition and instead have participating departments pay tuition. The program should also be designated as one-time. They also recommend adoption of the following supplemental report language:

The Department of General Services shall, by April 1, 2004, provide a status report to the chairs of the budget subcommittees, in each house and the Chair of the Joint Legislative Budget Committee of the state's procurement training and certification program. The report shall include: (1) descriptions of training courses conducted over the past 12 months, (2) the number of state staff attending each training course by department, (3) description and status of the state's certification program, (4) the number of state staff receiving certification over the past 12 months by department, (5) descriptions of proposed training courses to be provided over the next 12 months and the estimated number of state staff to be trained, and (6) descriptions of additional training courses needed and being developed.

The Department maintains that CSU would not agree to conduct the program if a reliable funding source is not provided. DGS also asserts that all departments would pay a portion of the procurement surcharge each year.

5. Notification Language. Three budget bill language provisions (Budget Item 1760-001-0666, Provisions 3, 5, and 6) allow DGS to augment its expenditure authority as required to provide services to departments. These provisions require DGS to notify DOF and the Legislature within 30 days **after** making such augmentations.

Other budget notifications generally require the administration to notify the Legislature 30 days **prior** to making budget adjustments.

The LAO recommends the budget bill language be revised to require DGS (or DOF) to notify the Legislature 30 days prior to making expenditure authority increases.

6. Master Plan for Central Plant.

a) The Governor's budget requests \$159.7 million (lease-revenue bonds) to renovate and expand the District Heating and Cooling System (central plant). Proposed spending would accommodate additional equipment and construct an 8 million gallon underground Thermal Energy Storage tank, new cooling towers, and an underground piping distribution system.

The LAO is concerned with providing funding for all phases of such a large complicated project in this budget. If the proposed funding is approved for this project, **the LAO recommends** *the inclusion of the following proposed budget bill language in Item 1760-301-0660 as a way to ensure the Legislature's oversight of the project:*

The Department of Finance will provide written notification to the Joint Legislative Budget Committee, within ten days of receipt, of any requests for an augmentation of project costs, change in project scope, and any related change in project schedule, for projects identified in Schedule (1).

Does the Subcommittee want to approve the LAO language?

b) An April 1 Finance Letter proposes to add language to the Central Plant project that would allow DGS to use "design-build" as a method to acquire the Central Plant project. **The LAO** is concerned with the use of "design-build" as a method of procurement because it does not necessarily result in a project being awarded to the lowest responsible bid, nor is the project scope fully defined at the outset of the project. However, notwithstanding these concerns the Legislature has authorized the use of design-build in other state projects.

LAO recommends *that the proposed budget bill language be amended to require DGS to use "lowest price" as a criteria when deciding which design-build team will be awarded the project.*

Does the Subcommittee want to adopt the Finance Letter?

Consent Issues:

7. Finance Letter: Technical Correction. This Finance Letter requests restoration of \$1.1 million (SRF) to restore funding that was incorrectly deleted from the DGS Budget.

The LAO concurs with this request.

8. Finance Letter: Reappropriation of Proposition 122 Funds. This Finance Letter requests reappropriation of Earthquake Safety and Public Building Rehabilitation Bond Fund of 1990 funds of \$2.4 million for local seismic grants that were reappropriated in 2001.

The LAO concurs with this request.

9. Finance Letter: Notification of change in 911 Emergency Services Program. The Finance Letter notices a change in the reimbursement of the City of Los Angeles for the purchase of equipment. This will be funded due to savings from delays in other program implementation.

The LAO concurs with this request.

10. Finance Letter: Reappropriations of Capital Outlay Funds. The April 1 Finance Letter proposes several reappropriations and the extension of the liquidation period for nine seismic projects.

The LAO concurs with this request.

1880 State Personnel Board

The State Personnel Board (SPB) has the authority to adopt civil service rules and regulations. These duties include, but are not limited to, adopting classifications within the State Civil Service System, conducting hearings and appeals on matters of discipline for civil service employees, and developing and administering the merit-based civil service hiring and promotional process.

The budget proposes \$16 million for SPB support in 2003-04, which is \$3.4 million, or 17 percent, below current-year estimated expenditures. The proposed expenditures consist of \$3 million (GF) and \$13 million in reimbursements from state departments and other government entities.

1. Finance Letter: Restoration of Positions. The budget proposed a reduction of \$3.8 million (GF) and 57 positions for SPB. This would result in a 53 percent decline in GF support from the current year, leaving \$3.1 million (GF) for the budget year. Activities funded by reimbursements would be unaffected. The budget notes that General Fund support for the following SPB functions would be retained:

- Hearing appeals of disciplinary actions.
- Developing exams for the civil service hiring process.
- Providing advice and assistance related to the Dymally-Alatorre Bilingual Services Act.

This Finance Letter requests an increase of \$825,000 (GF) and increased reimbursements of \$895,000 for a total increase of \$1.7 million. These funds are to support the reestablishment of 22.3 positions to correct technical errors in the budget, to fund the equal employment opportunity program, and to fund workload related to anticipated layoffs.

SB 1045 (Polanco), Chapter 1165, Statutes of 2002, required state and local governmental agencies to utilize specified methods for conducting employment outreach and recruitment programs. SPB should describe the extent to which they will meet these requirements in 2003-04 and beyond.

Has SPB identified their core constituencies and have they developed an outreach strategy to these constituencies?

What outreach media and information dissemination tools are being used?

Has SPB integrated telecommunications technologies and web-based information delivery in your outreach tools?

What strategies are being utilized to reach under-served communities?